FINANCIAL SECTION

for Fiscal Year ending June 30, 2004

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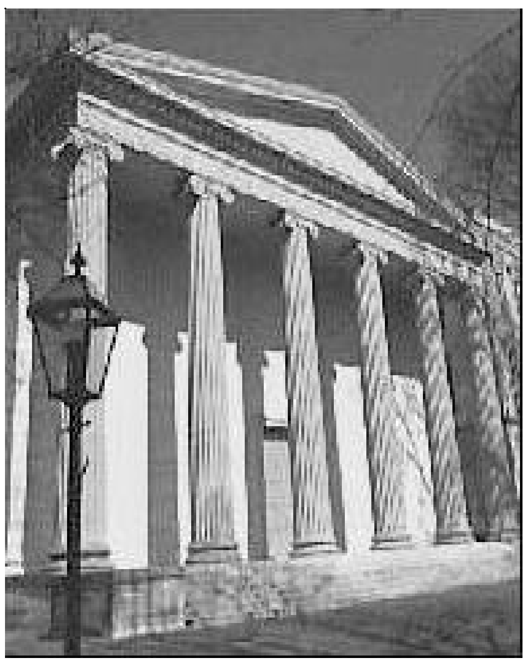

The Old State Capitol

Frankfort, Kentucky

Completed in 1830, this national historic landmark introduced Greek Revival architecture to the United States west of the Appalachian Mountains. The building served as the capitol of the Commonwealth of Kentucky from 1830 to 1910. Here Kentucky's leaders decided the course their state would take through the tumultuous nineteenth century.

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Teachers' Retirement System of the State of Kentucky
Frankfort, Kentucky

We have audited the accompanying statements of plan net assets of the Teachers' Retirement System of the State of Kentucky as of June 30, 2004 and 2003 and the related statements of changes in plan net assets for the years then ended. These component unit financial statements are the responsibility of the Teachers' Retirement System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the general purpose financial statements referred to above present fairly, in all material respects, the plan net assets of the Teachers' Retirement System of the State of Kentucky, a component unit of the Commonwealth of Kentucky, at June 30, 2004 and 2003 and the changes in its plan net assets for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated December 9, 2004 on our consideration of the Teachers' Retirement System of the State of Kentucky's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis on pages 15-18 are not a required part of the basic financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplemental information. However, we did not audit the information and express no opinion on it.

The financial section supporting schedules listed in the table-of-contents are presented for the purpose of additional analysis and are not a required part of the basic financial statements. These schedules are the responsibility of the System's management. Such schedules as of and for the year ended June 30, 2004 have been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, are fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

We did not audit the data included in the Introductory and Statistical Sections of the report and therefore express no opinion on them.

Charles T. Mitchell Co.

December 9, 2004

MANAGEMENT'S DISCUSSION AND ANALYSIS

This discussion and analysis of Kentucky Teachers' Retirement System's financial performance provides an overview of the defined benefit and medical insurance plans' financial year ended June 30, 2004. Please read it in conjunction with the respective financial statements, which begin on page 19.

USING THIS FINANCIAL REPORT

Because of the long-term nature of a defined benefit pension plan and medical insurance plan, financial statements alone cannot provide sufficient information to properly reflect the plan's ongoing plan perspective. The Statement of Plan Net Assets and Statement of Changes in Plan Net Assets (on pages 19-20) provide information about the activities of the defined benefit plan, medical insurance plan, and the tax-sheltered annuity plan as a whole. The Kentucky Teachers' Retirement System is the fiduciary of funds held in trust for its members.

The Schedule of Funding Progress (on pages 32-33) includes historical trend information about the actuarially funded status of each plan from a long-term, ongoing plan perspective and the progress made in accumulating sufficient assets to pay benefits and insurance premiums when due. The Schedule of Employer Contributions (on pages 33-34) presents historical trend information about the annual required contributions of employers and the contributions made by employers in relation to the requirement. These schedules provide information that contributes to understanding the changes over time in the funded status of the plans.

KENTUCKY TEACHERS' RETIREMENT SYSTEM AS A WHOLE

In the fiscal year ended June 30, 2004, Kentucky Teachers' Retirement System's combined plan net assets increased by $868.1 million – from $12,208.6 million to $13,076.7 million. The following summaries focus on plan net assets and changes in plan net assets of Kentucky Teachers' Retirement System's defined benefit plan, medical insurance plan, and the tax-sheltered annuity plan.

Summary of Plan Net Assets
(In Millions)

Categories	Defined Benefit Plan 2004	Defined Benefit Plan 2003	Defined Benefit Plan 2002	Medical Insurance Plan 2004	Medical Insurance Plan 2003	Medical Insurance Plan 2002	TOTAL* 2004	TOTAL* 2003	TOTAL* 2002
Cash & Investments	$13,486.8	$12,705.8	$12,255.8	$159.7	$170.4	$149.4	$13,646.5	$12,876.2	$12,405.2
Receivables	162.9	113.8	106.6	2.7	3.1	4.5	165.6	116.9	111.1
Capital Assets	3.4	3.6	3.8				3.4	3.6	3.8
Total Assets	$13,653.1	$12,823.2	$12,366.2	$162.4	$173.5	$153.9	$13,815.5	$12,996.7	$12,520.1
Total Liabilities	(733.5)	(780.7)	(603.4)	(5.8)	(8.0)	(7.8)	(739.3)	(788.7)	(611.2)
Plan Net Assets	$12,919.6	$12,042.5	$11,762.8	$156.6	$165.5	$146.1	$13,076.2	$12,208.0	$11,908.9

Summary of Changes In Plan Net Assets
(In Millions)

Categories	Defined Benefit Plan 2004	Defined Benefit Plan 2003	Defined Benefit Plan 2002	Medical Insurance Plan 2004	Medical Insurance Plan 2003	Medical Insurance Plan 2002	TOTAL* 2004	TOTAL* 2003	TOTAL* 2002
ADDITIONS									
Member's Contributions	$238.9	$233.4	$224.4	$53.9	$50.7	$46.2	$292.8	$284.1	$270.6
Employer's Contributions	382.3	341.1	303.5	53.3	77.2	95.3	435.6	418.3	398.8
Investment Income (net)	1,158.2	538.6	($520.2)	7.1	7.4	6.1	1,165.3	546.0	($514.1)
TOTAL ADDITIONS	$1,779.4	$1,113.1	$7.7	$114.3	$135.3	$147.6	$1,893.7	$1,248.4	$155.3
DEDUCTIONS									
Benefit Payments	$885.3	$817.1	$739.4				$885.3	$817.1	$739.4
Refunds	10.5	9.9	9.2				10.5	9.9	9.2
Administrative Expense	6.6	6.4	6.7	3.9	3.7	3.5	10.5	10.1	10.2
Insurance Expenses				119.3	112.2	101.5	119.3	112.2	101.5
TOTAL DEDUCTIONS	$902.4	$833.4	$755.3	$123.2	$115.9	$105.0	$1,025.6	$949.3	$860.3
Increase (Decrease) in Plan Net Assets	$877.0	$279.7	($747.6)	($8.9)	$19.4	$42.6	$868.1	$299.1	($705.0)

* These summaries do not include the 403(b) tax-shelter plan.

Plan net assets of the defined benefit plan increased by 7.3% ($12,919.6 million compared to $12,042.5 million). The increase is primarily due to gains in investment income; $1,158.2 million compared to $538.6 million, due to more favorable investment market conditions in general. These assets are restricted to providing monthly retirement allowances to members and their beneficiaries.

Plan net assets of the medical insurance plan decreased by 5% ($156.6 million compared to $165.5 million) primarily due to a decrease in the allotment from supplemental funding per actuary recommendation. Plan assets are restricted to providing hospital and medical insurance benefits to members and their spouses.

Defined Benefit Plan Activities

Member contributions increased $5.5 million. Retirement contributions are calculated by applying a percentage factor to salary and are paid in monthly by each member. Members may also pay contributions to repurchase previously refunded service credit or to purchase various types of elective service credit.

Employer contributions totaled $382.2 million; a net increase of $41.2 million over fiscal year 2002-2003 contributions.

Net investment income increased $619.6 million ($1,158.2 million gain at June 30, 2004 as compared to a $538.6 million gain at June 30, 2003). The increase in the fair value of investments is mainly due to more favorable market conditions for the year ended June 30, 2004 as opposed to the year ended June 30, 2003. This can be illustrated as follows:

(In Millions)	2004	2003	2002
Appreciation (depreciation) in fair value of investments – June 30, prior year	$ (361.6)	$ (479.3)	$ 471.7
Appreciation (depreciation) in fair value of investments – June 30, end of year	171.0	(361.6)	(479.3)
Change in net appreciation (depreciation) in fair value of investments	532.6	117.7	(951.0)
Net income (net of investment expenses)	395.0	396.1	409.1
Net gain on sale of investments	$ 230.5	$ 24.8	21.7
Investment Income (net) – June 30, end of year	1,158.1	538.6	$ (520.2)

Program deductions in 2003-2004 increased $68.9 million. The increase was caused principally by an increase of $68.2 million in benefit payments. Members who were drawing benefits as of June 2003 received an increase of 3% to their retirement allowances in July 2003. Also, there was an increase of 1,093 members and beneficiaries on the retired payroll as of June 30, 2004.

Medical Insurance Plan Activities

During the 2003-2004 fiscal year, member contributions increased $3.1 million and employer contributions decreased by $23.9 million over fiscal year 2003-2004. The member contribution increased due to an increase in the amount of covered payroll. The employer contribution was based on a 2.05% allocation of employer contributions as compared to 3% for fiscal year 2002-2003.

Program deductions increased $7.4 million explained almost totally by an increase in payment of insurance expenses of $7.1 million. The monthly premiums and medical/prescription claims increased for all retirees coupled with an increase of 830 in the number of retirees receiving premium subsidies.

Net investment income decreased $.3 million. This is due solely to the recognition of interest income. Since all investments for the Medical Insurance Plan are short term in nature, the recognition of appreciation in fair value is not feasible. This can be illustrated as follows:

(In Millions)	2004	2003	2002
Appreciation in fair value of investments – June 30, prior year	$ 0	$ 0	$ 0
Appreciation in fair value of investments – June 30 end of year	0	0	0
Net appreciation in fair value of investments	0	0	0
Net income (net of investment expense)	7.1	7.4	6.1
Net gain on sale of investments	0	0	0
Investment Income (net) – June 30	$ 7.1	$ 7.4	$ 6.1

HISTORICAL TRENDS

Accounting standards require that the statement of plan net assets state asset value at fair value and include only benefits and refunds due plan members and beneficiaries and accrued investment and administrative expenses as of the reporting date. Information regarding the actuarial funding status of the defined benefit plan and the medical insurance plan is provided in the Schedule of Funding Progress (on pages 32-33). The asset value, stated in the Schedule of Funding Progress, is determined by the System's independent actuary. The actuarial accrued liability is calculated using the projected unit credit cost method.

In the past, the defined benefit plan has experienced improvement year to year in its funding position with more than adequate assets to meet pension obligations. The 2003-2004 fiscal year reveals a decline in funding position due to declining financial markets and an increase in actuarial liability. Even under these adverse conditions, the defined benefit plan continues to be well funded.

The medical insurance plan is not as vulnerable to adverse market conditions since its assets are all short term in nature and less likely to experience huge fluctuations. Although, the plan continues to have a large unfunded actuarial liability, the current obligations are being met by current funding.

Annual required contributions of the employers and contributions made by the employees in relation to the required contributions are provided in the Schedule of Employer Contributions (on pages 33-34). This schedule indicates that employers are generally meeting their responsibilities to provide resources to the plans.

Statement of Plan Net Assets
As of June 30, 2004 and 2003

	Defined Benefit Plan 2004	Defined Benefit Plan 2003	Medical Insurance Plan 2004	Medical Insurance Plan 2003	403(b) Tax Shelter 2004	403(b) Tax Shelter 2003	TOTAL 2004	TOTAL 2003
ASSETS								
Cash	$ 3,825,270	$ 1,736,195					$ 3,825,270	$ 1,736,195
Prepaid expenses	208,394	197,229					208,394	197,229
Receivables								
Contributions	28,142,243	28,749,028	$ 2,739,138	$ 3,112,990			30,881,381	31,862,018
State of Kentucky	22,933,239	20,462,340					22,933,239	20,462,340
Investment income	61,238,746	62,412,661			$ 19	$ 6,850	61,238,765	62,419,511
Investment sales receivable	49,294,598	418,766					49,294,598	418,766
Installment account receivable	1,278,604	1,734,891					1,278,604	1,734,891
Other receivables		4,114						4,114
Total receivables	162,887,430	113,781,800	2,739,138	3,112,990	19	6,850	165,626,587	116,901,640
Investments, at fair value (See Note 4)								
Short term investments	842,038,540	662,209,877	159,700,807	170,455,643	560,653	84,480	1,002,300,000	832,750,000
Bonds and mortgages	4,376,987,369	5,042,133,967				505,781	4,376,987,369	5,042,639,748
Common stock	7,215,138,496	5,864,486,294					7,215,138,496	5,864,486,294
Real estate	365,389,453	358,280,904					365,389,453	358,280,904
Total investments	12,799,553,858	11,927,111,042	159,700,807	170,455,643	560,653	590,261	12,959,815,318	12,098,156,946
Invested security lending collateral	683,199,087	776,713,902					683,199,087	776,713,902
Capital assets, at cost net of accumulated depreciation of $1,527,920 (See Note 2)	3,450,696	3,633,640					3,450,696	3,633,640
Total assets	13,653,124,735	12,823,173,808	162,439,945	173,568,633	560,672	597,111	13,816,125,352	12,997,339,552
LIABILITIES								
Liabilities								
Accounts payable	1,139,729	1,064,850		358,061			1,139,729	1,422,911
Treasurer's unredeemed checks	8,933	28,396					8,933	28,396
Insurance claims payable			5,798,772	7,664,801			5,798,772	7,664,801
Compensated absences payable	616,176	637,734					616,176	637,734
Revenues collected in advance		873	7,009	9,196			7,009	10,069
Investment purchases payable	48,604,223	2,220,223					48,604,223	2,220,223
Obligations under securities lending	683,199,087	776,713,902					683,199,087	776,713,902
Total liabilities	733,568,148	780,665,978	5,805,781	8,032,058			739,373,929	788,698,036
Net assets held in trust for pension & post-employment healthcare benefits:	$12,919,556,587	$12,042,507,830	$ 156,634,164	$ 165,536,575	$ 560,672	$ 597,111	$ 13,076,751,423	$12,208,641,516

(See Required Supplemental Schedule 1 for a schedule of funding progress.)

The accompanying notes are an integral part of these financial statements.

Statement of Changes in Plan Net Assets
For the Years Ended June 30, 2004 and 2003

	Defined Benefit Plan		Medical Insurance Plan		403(b) Tax Shelter		TOTAL	
	2004	2003	2004	2003	2004	2003	2004	2003
ADDITIONS								
Contributions								
Employer	$ 382,280,099	$ 341,132,900	$ 53,346,747	$ 77,235,407			$ 435,626,846	$ 418,368,307
Member	238,922,086	233,429,797	53,903,551	50,718,084			292,825,637	284,147,881
Total contributions	621,202,185	574,562,697	107,250,298	127,953,491	0	0	728,452,483	702,516,188
Investment Income								
Net appreciation (depreciation) in fair value of Investments	763,180,625	142,546,371			$ (5,781)	$ 2,790	763,174,844	142,549,161
Interest	249,055,825	269,115,819	7,127,109	7,391,671	10,826	16,460	256,193,760	276,523,950
Dividends	118,486,962	99,217,149					118,486,962	99,217,149
Rental income, net	31,532,501	31,207,052					31,532,501	31,207,052
Securities lending, gross earnings	5,988,422	9,811,225					5,988,422	9,811,225
Gross investment income	1,168,244,335	551,897,616	7,127,109	7,391,671	5,045	19,250	1,175,376,489	559,308,537
Less investment expense	(4,616,663)	(4,119,182)					(4,616,663)	(4,119,182)
Less securities lending expense	(5,444,984)	(9,226,360)					(5,444,984)	(9,226,360)
Net investment income	1,158,182,688	538,552,074	7,127,109	7,391,671	5,045	19,250	1,165,314,842	545,962,995
Total additions	1,779,384,873	1,113,114,771	114,377,407	135,345,162	5,045	19,250	1,893,767,325	1,248,479,183
DEDUCTIONS								
Benefits	885,286,089	817,064,668			41,484	47,395	885,327,573	817,112,063
Refunds of contributions	10,471,607	9,951,410	12,150	7,808			10,483,757	9,959,218
Insurance expenses			119,297,358	112,173,662			119,297,358	112,173,662
Administrative expense	6,578,420	6,388,183	3,970,310	3,672,425			10,548,730	10,060,608
Total deductions	902,336,116	833,404,261	123,279,818	115,853,895	41,484	47,395	1,025,657,418	949,305,551
Net increase (decrease)	877,048,757	279,710,510	(8,902,411)	19,491,267	(36,439)	(28,145)	868,109,907	299,173,632
Net assets held in trust for pension & post employment healthcare benefits								
Beginning of year	12,042,507,830	11,762,797,320	165,536,575	146,045,308	597,111	625,256	12,208,641,516	11,909,467,884
Ending of year	$ 12,919,556,587	$12,042,507,830	$ 156,634,164	$165,536,575	$ 560,672	$ 597,111	$13,076,751,423	$12,208,641,516

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements
Years Ended June 30, 2004 and 2003

Note 1: Description of Plan

A. REPORTING ENTITY

The Teachers' Retirement System of the State of Kentucky (KTRS) was created by the 1938 General Assembly and is governed by Chapter 161 Section 220 through Chapter 161 Section 990 of the Kentucky Revised Statutes (KRS). KTRS is a blended component unit of the Commonwealth of Kentucky and therefore is included in the Commonwealth's financial statements. KTRS is a cost-sharing multiple-employer defined benefit plan established to provide pension benefit plan coverage for local school districts and other public educational agencies in the state.

B. PARTICIPANTS

As of June 30, 2004 a total of 199 employers participated in the plan. Employers are comprised of 176 local school districts, 17 Department of Education Agencies and other educational organizations, 5 universities and also the Kentucky Community and Technical College System.

According to KRS 161.220 " . . . any regular or special teacher, or professional occupying a position requiring certification or graduation from a four (4) year college or university . . . " is eligible to participate in the System. The following illustrates the classifications of members:

Active contributing members:	2004	2003
Vested	40,446	38,961
Non-vested	31,504	32,136
Inactive members, vested	3,003	5,478
Retirees and beneficiaries currently receiving benefits	35,803	34,708
Total members, retirees and beneficiaries	**110,756**	**111,283**

C. BENEFIT PROVISIONS

Members become vested when they complete five (5) years of credited service. To qualify for monthly retirement benefits, payable for life, members must either:

1.) Attain age fifty-five (55) and complete five (5) years of Kentucky service, or

2.) Complete 27 years of Kentucky service.

Note 1: Description of Plan continued . . .

Participants that retire before age 60 with less than 27 years of service receive reduced retirement benefits. Non-university members receive monthly payments equal to two (2) percent (service prior to July 1, 1983) and two and one-half (2.5) percent (service after July 1, 1983) of their final average salaries for each year of credited service. University employees receive monthly benefits equal to two (2) percent of their final average salary for each year of credited service. The final average salary is the member's five (5) highest annual salaries except members at least 55 with 27 or more years of service may use their (3) three highest annual salaries. New members (including second retirement accounts started) after July 1, 2002 will receive monthly benefits equal to 2% of their final average salary for each year of service if, upon retirement, their total service is less than ten years. New members after July 1, 2002 who retire with ten or more years of total service will receive monthly benefits equal to 2.5% of their final average salary for each year of service, including the first ten years. In addition, members who retire July 1, 2004 and later with more than 30 years of service will have their multiplier increased for all years over 30 from 2.5% to 3.0% to be used in their benefit calculation.

The system also provides disability benefits for vested members at the rate of sixty (60) percent of the final average salary. A life insurance benefit, payable upon the death of a member, is $2,000 for active contributing members and $5,000 for retired or disabled members.

Cost of living increases are one and one-half (1.5) percent annually. Additional ad hoc increases, and any other benefit amendments must be authorized by the General Assembly.

Note 2: Summary of Significant Accounting Policies

A. BASIS OF ACCOUNTING
The financial statements are prepared on the accrual basis of accounting. Member contributions and employer matching are recognized in the fiscal year due. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

B. CASH
KTRS has three cash accounts. At June 30, 2004, the pension cash account totaled $1,621,676 the administrative expense fund cash account was $1,170,223 and the life insurance cash account totaled $1,033,370; therefore, the carrying value of cash was $3,825,270 and the corresponding bank balance was $5,933,202. The variance is primarily due to outstanding checks and items not processed by the bank on June 30, 2004.

C. CAPITAL ASSETS
Capital assets are recorded at historical cost less straight-line accumulated depreciation. The classes of capital assets are furniture and equipment, the KTRS office buildings and land. Furniture and equipment are depreciated over an average useful life of five to seven years. The office buildings are depreciated over forty years.

Note 2: Summary of Significant Accounting Policies continued . . .

D. INVESTMENTS

Plan investments are reported at fair value. Fair value is the amount that a plan can reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller. Short-term securities are carried at cost, which approximates fair value. Fixed income and common and preferred stocks are generally valued based on published market prices and quotations from national security exchanges and securities pricing services. Real estate is primarily valued based on appraisals performed by independent appraisers.

Purchase and sales of debt securities, equity securities, and short-term investments are recorded on the trade date. Real estate equity transactions are recorded on the settlement date. Upon sale of investments, the difference between sales proceeds and cost is reflected in the statement of changes in plan net assets.

Investment expenses consist of investment manager and consultant fees along with fees for custodial services.

E. COMPENSATED ABSENCES

Expenses for accumulated vacation days and compensatory time earned by the System's employees are recorded when earned. Upon termination or retirement, employees of the system are paid for accumulated vacation time limited to 450 hours and accumulated compensatory time limited to 200 hours. As of June 30, 2004 and 2003 accrued compensated absences were $616,176 and $637,734.

F. RISK MANAGEMENT

Destruction of assets, theft, employee injuries and court challenges to administrative policy are among the various risks to which the system is exposed. In order to cover such risks the system carries appropriate insurance policies such as fire and tornado, employee bonds, fiduciary liability, worker's compensation and equipment insurance.

G. OTHER RECEIVABLES

KTRS now allows qualified purchases of service credit to be made by installment payments not to exceed a five-year period. Revenue is recognized in the initial year of the installment contract agreement. The June 30, 2004 and 2003 installment contract receivables were $1,278,604 and $1,734,891.

H. USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

I. INCOME TAXES

The defined benefit plan is organized as a tax-exempt retirement plan under the Internal Revenue Code. The tax sheltered annuity plan is no longer continued and will be fully terminated when all lifetime annuities have expired. The system's management believes that it has operated the plans within the constraints imposed by federal tax law.

Note 3: Contributions and Reserves

A. CONTRIBUTIONS

Contribution rates are established by Kentucky Revised Statutes. Members are required to contribute 9.855% of their salaries to the System. University members are required to contribute 8.375% of their salaries. KRS 161.580 allows each university to reduce the contribution of its members by 2.215%; therefore, university members contribute 6.16% of their salary to KTRS.

The Commonwealth of Kentucky is required to contribute 13.105% of salaries for its non-university members and 13.84% of salaries for university members.

The member and employer contributions consist of pension contributions and post-retirement contributions. The post-retirement contribution .75% finances KTRS' retiree medical insurance plan. In addition to the .75% contribution, employers and the Commonwealth contribute 1.30% for a total of 2.05% to the medical insurance plan.

If an employee leaves covered employment before accumulating five (5) years of credited service, accumulated employee contributions plus interest are refunded to the employee upon the member's request.

B. RESERVES

Member Reserve

This fund was established by KRS 161.420(2) as the Teacher Savings Fund and consists of contributions paid by university and non-university members. The fund also includes interest authorized by the Board of Trustees from Unallocated Reserves. The accumulated contributions of members that are returned upon withdrawal or paid to the estate or designated beneficiary in the event of death are paid from this fund. Upon retirement, the member's contributions and the matching state contributions are transferred from this fund to Benefit Reserves, the fund from which retirement benefits are paid.

Employer Reserve

This fund was established by KRS 161.420(3) as the State Accumulation Fund and receives state appropriations to the Retirement System. The state matches an amount equal to members' contributions. State appropriations during the year are based on estimates of members' salaries. At year-end when actual salaries are known, the required state matching is also realized by producing either a receivable from or a payable to the State of Kentucky. The analysis of fiscal years 2004 and 2003 has resulted in a receivable (under-appropriation) from the state in each of those years.

Benefit Reserve

This fund was established by KRS 161.420(4) as the Allowance Reserve Fund, the source for retirement, disability, and survivor benefits paid to members of the System. These benefits are paid from the retired members' contributions until they are exhausted, at which time state

Note 3: Contributions and Reserves continued . . .

matching contributions are used to pay the benefits. After an individual member's contributions and the state matching contributions have been exhausted, retirement benefits are paid from monies transferred from Unallocated Reserves.

Unallocated Reserve

This fund was established by KRS 161.420(6) as the Guarantee Fund to collect income from investments, state matching contributions of members withdrawn from the System, and state matching contributions for cost of living adjustments (COLAs). In addition, it receives money for which disposition is not otherwise provided. This fund provides interest to the other funds, benefits in excess of both members' and state matching contributions, monies for administrative expenses of the System, and deficiencies not covered by the other funds.

Administrative Expense Reserve

This fund was established by KRS 161.420(1) as the Expense Fund. Monies transferred to this fund from Unallocated Reserves are used to pay the administrative expenses of the System.

Life Insurance Reserve

This fund was established pursuant to the provisions of KRS 161.655 to provide a life insurance benefit to retired and active members of the Kentucky Teachers' Retirement System. This benefit is financed by KTRS employer contributions that are actuarially determined.

Note 4: Deposits With Financial Institutions and Investments (Including Repurchase Agreements)

A. Summary of Investments

The following disclosures are meant to help the users of KTRS's financial statements assess the risks KTRS takes in investing public funds. The Board of Trustees and the Investment Committee are guided by asset allocation parameters that the Board approves through its powers defined in KRS 161.430. The parameters as outlined in Title 102, Chapter 1.175, Section 2 of the Kentucky Administrative Regulations are as follows:

- There shall be no limit on the amount of investments owned by the System that are guaranteed by the U.S. Government.
- Not more than thirty-five percent (35%) of the assets of the System at book value shall be invested in corporate debt obligations.
- Not more than sixty percent (60%) of the assets of the System at book value shall be invested in common stocks or preferred stocks. Not more than twenty-five percent (25%) of the assets of the System at book value shall be invested in a stock portfolio designed to replicate a general, United States stock index.

Note 4: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

- Not more than ten percent (10%) of the assets of the System at book value shall be invested in real estate. This would include real estate equity, real estate lease agreements, mortgages on real estate that are not guaranteed by the U.S. Government, and shares in real estate investment trusts.
- Not more than one percent (1%) of the assets of the System at book value shall be invested in venture capital investments, providing at least seventy-five percent (75%) of such investments must be in-state.
- Not more than ten percent (10%) of the assets of the System at book value shall be invested in any additional category or categories of investments. The Board of Trustees shall approve by resolution such additional category or categories of investments.

The chart on the following page represents the fair values of the investments of the Kentucky Teachers' Retirement System for June 30, 2004.

The KTRS bank balance consists of cash totaling $3,825,270 which is fully insured or collateralized with securities by KTRS or its agent in the entity's name.

B. Securities Lending

Section 161.430 of the Kentucky Revised Statutes empowers the Board of Trustees with complete fiduciary responsibility for the funds of the System. The System operates a securities lending program in which it temporarily lends securities to qualified agents in exchange for a net fee and high quality collateral. U.S. Government and agency securities and selected domestic stocks and bonds are the types of securities that are lent. The System's securities sub-custodian, The Bank of New York, acts as lending agent in exchanging securities for collateral. The collateral has a value of not less than 102% of the market value of the lent securities plus any accrued, unpaid distributions. The collateral consists of cash, marketable U.S. Government securities, and selected marketable U.S. Government agency securities approved by the System. Cash collateral is invested in short-term obligations fully guaranteed by the United States Government or select Government agencies and Government Repurchase Agreements with qualified agents. The System cannot pledge or sell collateral securities received unless the borrower defaults. The lending agent also indemnifies the System from any financial loss associated with a borrower's default and collateral inadequacy. As of June 30, 2004, the weighted average maturity of cash collateral investments was one day. At fiscal year end, the System has no credit risk exposure to borrowers, since the amounts the System owes the borrowers exceeds the amounts the borrowers owe the System.

Note 4: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

Schedule of Investments

	June 30, 2004	June 30, 2003
Short Term Investments		
Repurchase Agreements	$ 1,002,300,000	$ 832,750,000
Total Short Term Investments	$ 1,002,300,000	$ 832,750,000
Bonds and Mortgages		
U.S. Government Obligations		
Treasury Notes & Bonds	$ 1,106,798,881	$ 1,470,166,548
Agencies	1,101,943,172	1,142,583,581
GNMA (Single Family)	56,075,979	109,998,128
Other Miscellaneous	163,517,120	194,454,418
Total U.S. Government Obligations	$ 2,428,335,152	$ 2,917,202,675
Corporate Bonds		
Industrial	$ 655,562,791	$ 716,793,926
Finance	1,001,883,461	1,072,531,279
Utility Bonds (Except Telephone)	128,647,999	139,274,389
Telephone Bonds	109,896,206	121,055,802
Total Corporate Bonds	$ 1,895,990,457	$ 2,049,655,396
Other Fixed Income Investments		
FHA and VA Single Family Mortgages	$ 34,182	$ 113,900
Project Mortgages (FHA & GNMA)	26,760,755	47,863,253
State and Local Government Issues	25,866,823	27,804,524
Total Other Investments	$ 52,661,760	$ 75,781,677
Total Bonds and Mortgages	$ 4,376,987,369	$ 5,042,639,748
Stocks	$ 7,215,138,496	$ 5,864,486,294
Real Estate	365,389,453	358,280,904
Total Investments	$ 12,959,815,318	$ 12,098,156,946

This schedule does not include $683,199,087 securities lending collateral.

Note 4: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

C. Summary of Categorized Investments

The following chart categorizes KTRS's investments, which gives an indication of the level of risk assumed by KTRS at June 30, 2004. Category 1 includes investments that are insured or registered or for which the securities are held by KTRS' custodial agent in KTRS' name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counter party's trust department or agent in KTRS' name. Category 3 includes securities purchased by and held by the System's custodial agent. The agent loans securities owned by the System with the simultaneous receipt of cash collateral for the loaned securities. Cash collateral is reinvested in accordance with the System's securities lending agreement. All securities purchased with cash collateral are segregated by the custodial agent and held in the name of KTRS.

Included in Category 1 are individual repurchase agreements which are ordered by KTRS under the terms of master repurchase agreements with various qualified brokers. The terms of these master repurchase agreements are dictated by KTRS. The repurchase agreements and their supporting collateral are held by the custodial agent's correspondent bank in an account identified by the custodian's name and KTRS' nominee name. This account is unique to KTRS. The master repurchase agreements require that the supporting collateral have a market value of at least 100% of the value of the repurchase agreements. Also, listed among the Other Government Guaranteed Fixed Income Investments are mortgages which are either securitized or unsecuritized, but all are insured through various Federal or State Agencies (FHA, GNMA, VA).

Summary of Categorized Investments
as of June 30, 2004

	Total Fair Value
Investments - Category 1	
Repurchase Agreements	$ 1,002,300,000
U.S. Government Obligations	$ 1,775,933,970
Corporate Bonds	1,895,990,457
State and Local Government Issues	25,866,823
Common Stocks	7,208,776,947
Investments - Category 3	
Securities Lending Short-Term Collateral Repurchase Agreements	$ 683,199,087
SUBTOTAL	$ 12,592,067,284
Investments - Not Categorized	
Investments held by broker dealers under securities loans with cash collateral	
U.S. Government Obligations	$ 656,382,690
Corporate Bonds	6,361,549
Common Stocks	22,813,429
Other Government Guaranteed Fixed Income Investments	
Real Estate	$ 365,389,453
TOTAL	$ 13,643,014,405

Note 5: Medical Insurance Plan & Post-Employment Benefits

A. PLAN DESCRIPTION

In addition to the required pension benefits described in Note 1, Kentucky Revised Statute 161.675 allows KTRS to provide post-retirement healthcare benefits to members and dependents. To be eligible for medical benefits, the member must have retired either for service or disability, attain age 55 with 5 years of Kentucky service or had 27 years of Kentucky service.

The KTRS self-insured plan is limited to KTRS members and spouses at least the age of 65. All KTRS members under the age of 65 are offered commercial insurance through a state insurance purchasing pool administered by the Kentucky Personnel Cabinet. The Personnel Cabinet's primary function is to negotiate contracts with health plans to obtain the best price for persons covered. KTRS members were given a supplement to be used for payment of their health insurance premium. The amount of the member's supplement was based on the member's service credit and age. Premiums over the monthly supplement are paid by the member. The system bears no risk for excess claims expenses under the commercial insurance coverage.

KTRS members and spouses at least age 65 in the KTRS self-insured plan are also given a supplement based on service credit. Members with 20 or more years of service received the highest supplement.

At June 30, 2004, KTRS insurance covered 28,584 retirees and 6,281 dependents.

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The Medical Insurance Plan financial statements are prepared using the accrual basis of accounting. Member contributions and employer matching are recognized in the fiscal year due. Healthcare premiums charged to retired members are recognized when due and any premiums collected in advance are recognized as a liability.

Method Used to Value Investments

Since the investments are all short-term investments they are reported at cost, which is fair value.

C. CONTRIBUTIONS

The post-retirement healthcare provided by KTRS is financed on a pay-as-you-go basis. In order to fund the post-retirement healthcare benefit, one and five tenths percent (1.5%) of the gross annual payroll of all active members is contributed. One-half (1/2) of this amount is derived from member contributions and one-half (1/2) from state appropriation. Also, the premiums collected from retirees as described in the plan description help meet the medical expenses of the plan.

Note 5: Medical Insurance Plan & Post-Employment Benefits continued . . .

Since medical expenses have skyrocketed in the last decade, it has become increasingly difficult to meet the expenses of the retiree health insurance program. To fund the plan, the state legislature has approved additional funding of 1.30% of payroll from the employer matching contribution to the Medical Insurance Plan.

D. INCURRED BUT NOT REPORTED CLAIMS LIABILITIES

July 1, 1991 KTRS became self-insured assuming all liability for post-retirement healthcare costs. Effective January 1, 1997, insurance plan participants under age 65 were offered insurance through a state purchasing pool. KTRS recognizes estimates of liabilities for self-insured unpaid claims that have incurred (both reported and unreported) using the development method. This method uses past observed patterns of time between the date the claim is incurred and the date the claim is paid to estimate incurred claims from available paid claim information. The following schedule shows the change in the claims and liability and the claims activity for the years ended June 30, 2004 and 2003.

	Fiscal Year 2004	Fiscal Year 2003
Beginning Unpaid Claims Liability	$ 7,664,801	$ 7,879,932
Claims Incurred		
Current Year	121,341,666	113,003,765
Increase (Decrease) in Prior Years	(2,044,308)	(830,103)
Total Incurred Claims	$ 119,297,358	$ 112,173,662
Claims Paid		
Current Year	$ 116,547,744	$ 106,297,426
Prior Years	4,615,643	6,091,367
Total Payments	$ 121,163,387	$ 112,388,793
Ending Unpaid Claims Liability	$ 5,798,772	$ 7,664,801

E. ADMINISTRATIVE EXPENSES

The total administrative expenses of $3,970,311 are processing fees paid to third party administrators.

Note 6: 403(b) Tax-Sheltered Annuity Plan

A. Plan Description

KTRS has, in prior years, administered a salary deferral program as permitted by section 403(b) of the Internal Revenue Code. Under this program members were able to voluntarily defer a portion of their compensation within the limits established by the applicable laws and regulations. However, the System's Board of Trustees determined that the cost of providing the necessary services to assure the System of continuing compliance with these laws and regulations was not economically feasible due to the limited participation in the program by the System's members. The Board decided, therefore, to discontinue offering the program as of April 30, 1997. Members who were not receiving annuities from their account as of April 30, 1997, were able to transfer their respective accounts directly into other tax-sheltered plans on a tax-free basis. As of June 30, 2004, the forty members who are receiving annuities will continue to receive distributions according to the terms of their respective elections.

B. Summary of Significant Policies

Basis of Accounting

The Tax-sheltered Annuity Plan financial statements are prepared using an accrual basis of accounting. Contributions are no longer being accepted into the plan, therefore, there are no receivables to be recognized.

Method Used to Value Investments

The short-term investments are reported at cost, which approximates fair value. A bond is reported at fair market value.

Note 7: Pension Plan for Employees of the System

Full-time employees of Kentucky Teachers' Retirement System (KTRS) participate in either KTRS or Kentucky Employees Retirement System. Both plans are multiple-employer cost sharing defined benefit pension plans. All KTRS employees in positions requiring a four-year degree are covered under KTRS. The contribution rates and required employer matching are the same as those of state agency employers in the system. These rates, the plan description and funding policy are fully disclosed in the notes to the financial statements of this KTRS CAFR.

The System's annual required contributions for KTRS employee members years ended June 30, 2004 and June 30, 2003 were $359,370 and $342,927 respectively.

All other KTRS employees are covered under the Kentucky Employee Retirement System (KERS) in the Non-Hazardous Employees Pension Plan. The plan provides for retirement, disability, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Per KRS 61.565(3), contribution rates shall be determined by the Board on the basis of an annual actuarial valuation. Rates may be amended by the Board as needed. The System's administrative budget and employer contribution rates are subject to the approval of the Kentucky General Assembly. Employee contribution rates are set by the statute and may be changed only by the Kentucky General Assembly.

Members of KERS were required to contribute 5% of their annual creditable compensation for both years ending June 30, 2004 and June 30, 2003. As the employer, KTRS is required to contribute the annual actuarially determined rate of the creditable compensation. The actuarial rate for both years ended June 30, 2004 and June 30, 2003 was 5.89%; and the System's annual required contributions to KERS were $123,483 and $75,749.

KERS issues a publicly available financial report that may be obtained by writing Kentucky Retirement System, 1260 Louisville Road, Frankfort, Kentucky 40601-6124.

Required Supplemental Schedule
Defined Benefit Plan
Schedule of Funding Progress
(dollar amounts in millions)

VALUATION YEAR JUNE 30	ACTUARIAL VALUE OF ASSETS	ACTUARIAL ACCRUED LIABILITIES	UNFUNDED ACTUARIAL ACCRUED LIABILITIES (UAAL)	FUNDED RATIO	COVERED PAYROLL	UAAL AS A % OF COVERED PAYROLL
	a	b	(b-a)	(a/b)	c	[(b-a)/c]
1999	$ 11,958.6	$ 12,288.2	$ 329.6	97.3%	$ 2,041.4	16.1%
2000	12,759.6	13,330.4	570.8	95.7	2,133.7	26.8
2001	13,299.2	14,642.1	1,342.9	90.8	2,213.8	60.7
2002	13,588.8	15,695.6	2,106.8	86.6	2,313.7	91.1
2003	13,863.8	16,594.8	2,731.0	83.5	2,497.7	109.3
2004	14,255.1	17,617.6	3,362.5	80.9	2,641.5	127.3

The amounts reported in this schedule of funding progress do not include assets or liabilities for post-employment healthcare benefits, nor are the assets and liabilities of the tax-sheltered annuity plan included.

Required Supplemental Schedule
Defined Benefit Plan
Schedule of Employer Contributions
(dollar amounts in millions)

FISCAL YEAR ENDED JUNE 30	ANNUAL REQUIRED CONTRIBUTIONS	PERCENTAGE CONTRIBUTED
1999	$ 288.5	100 %
2000	311.3	100
2001	262.8	100
2002	284.8	100
2003	322.0	100
2004	364.4	100

Required Supplemental Schedule
Medical Insurance Plan
Schedule of Funding Progress
(dollar amounts in millions)

VALUATION YEAR JUNE 30	ACTUARIAL VALUE OF ASSETS	ACTUARIAL ACCRUED LIABILITIES	UNFUNDED ACTUARIAL ACCRUED LIABILITIES (UAAL)	FUNDED RATIO	COVERED PAYROLL	UAAL AS A % OF COVERED PAYROLL
	a	**b**	**(b-a)**	**(a/b)**	**c**	**[(b-a)/c]**
2000	$ 54.0	$ 2,202.0	$ 2,148.0	2.5%	$ 2,133.7	100.7%
2001	103.4	2,531.0	2,427.6	4.1	2,213.8	109.7
2002	146.0	2,806.0	2,660.0	5.2	2,313.7	114.9
2003	165.5	2,886.0	2,720.5	5.7	2,497.7	108.9
2004	158.9	3,166.6	3,007.7	5.0	2,641.5	113.9

The amounts reported in this schedule of funding progress do not include assets or liabilities for the defined benefit plan, nor are the assets and liabilities of the tax-sheltered annuity plan included.

Required Supplemental Schedule
Medical Insurance Plan
Schedule of Employer Contributions
(dollar amounts in millions)

FISCAL YEAR ENDED JUNE 30	ANNUAL REQUIRED CONTRIBUTIONS	PERCENTAGE CONTRIBUTED
2000	$ 48.9	100%
2001	92.4	100
2002	95.3	100
2003	77.2	100
2004	53.3	100

Notes to Required Supplementary Information

Note 1: Description of Schedule of Funding Progress

Defined Benefit Plan

The schedule of Funding Progress summarizes the actuarial value of the System's assets and actuarial accrued liability as of June 30, 2004, and each of the preceding five years. The data presented in the schedule were obtained from the System's independent actuary's annual valuation report for each year presented.

Expressing the actuarial value of assets as a percentage of the actuarial accrued liabilities provides an indication whether the system is becoming financially stronger or weaker. Generally, the greater the percentage, the stronger the retirement system. Trends in unfunded actuarial accrued liabilities and annual covered payroll are both affected by inflation. Expressing the unfunded actuarial accrued liabilities as a percentage of annual covered payroll aids analysis of progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the retirement system.

Medical Insurance Plan

The schedule of Funding Progress summarizes the actuarial value of the System's assets and actuarial accrued liability as of June 30, 2004 and each of the preceeding four years. The data presented in the schedule were obtained from the System's independent actuary's annual valuation report for each year presented.

Expressing the actuarial value of assets as a percentage of the actuarial accrued liabilities provides an indication whether the system is becoming financially stronger or weaker. Generally, the greater the percentage, the stronger the plan. Trends in unfunded actuarial accrued liabilities and annual covered payroll are both affected by inflation. Expressing the unfunded actuarial accrued liabilities as a percentage of annual covered payroll aids analysis of progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the plan.

Note 2: Actuarial Methodologies and Assumptions

Defined Benefit Plan

A. Methodologies

The promised benefits of the System are included in the actuarially calculated contribution rates, which are developed using the unit credit actuarial cost method with projected benefits. The actuarial value of assets was determined using the method illustrated in the Actuarial Value of Assets table. Gains and losses are reflected in the unfunded accrued liability that is being amortized by regular annual contributions as a level percentage of payroll within a 30-year period using an open amortization approach. The five (5) year smoothed market approach is used for asset valuation.

Actuarial Value of Assets

(1)	Actuarial Value of Assets on June 30, 2003		$	13,863,786,244
(2)	2003/2004 Net Cash Flow			
	a.	Contributions		603,273,498
	b.	Disbursements		891,747,723
	c.	Net Cash Flow (2)a - (2)b		(288,474,225)
(3)	Expected Investment Return [(1) x .075] + [(2)c x .0375]			1,028,966,185
(4)	Expected Actuarial Value of Assets on June 30, 2004 (1) + (2)c + (3)			14,604,278,204
(5)	Market Value of Assets on June 30, 2004			12,858,540,479
(6)	Excess of Market Value over Expected Actuarial Value (5) - (4)			(1,745,737,725)
(7)	20% Adjustment towards Market Value .20 x (6)			(349,147,545)
(8)	Actuarial Value of Assets on June 30, 2004 (4) + (7)		$	14,255,130,659
(9)	Rate of Return on Actuarial Value			4.96%

B. Assumptions

Significant actuarial assumptions employed by the actuary for the funding purposes as of June 30, 2004, the most recent updated actuarial information include:

* Assumed inflation rate	4.0%
* Assumed investment rate	7.5%
* Assumed projected salary increases	4.0% - 8.1%
* Assumed post retirement benefit increase	1.5%

Note 2: Actuarial Methodologies and Assumptions continued . . .

Medical Insurance Plan

A. Methodologies

The actuarial value of assets is determined by using the market value as provided by KTRS. Compliance with applicable current or future accounting standards may require use of different actuarial methods or assumptions. For purposes of estimating the amortization, a 3.5% salary scale is used.

B. Assumptions

The actuarial value of assets is determined by using the market value as provided by KTRS. Compliance with applicable current or future accounting standards may require use of different actuarial methods or assumptions. For purposes of estimating the amortization, a 3.5% salary scale is used.

*	Assumed Discount Rate	7.5%
*	Assumed Plan Asset Return Rate	7.5%
*	Assumed Pre-Medicare Benefit Cost Trend Rate	12.4%
*	Assumed Post-Medicare Benefit Cost Trend Rate	13.5%
*	Assumed Ulitimate Cost Trend Rate	5.0%
*	Assumed Ulitimate Cost Trend Rate Achieved:	
	- Pre-Medicare 2012	
	- Post-Medicare 2011	

Supporting Schedule 1

Schedule of Administrative Expenses
Year Ended June 30, 2004

ADMINISTRATIVE EXPENSES	YEAR ENDED JUNE 30, 2004
Salaries	$ 4,785,493
Other Personnel Costs	299,500
Professional Services & Contracts	210,124
Utilities	54,754
Rentals	16,562
Maintenance	179,769
Postage & Related Services	276,908
Printing	114,705
Insurance	79,600
Miscellaneous Services	120,503
Telecommunications	29,998
Computer Services	49,579
Supplies	49,092
Depreciation	182,944
Travel	30,905
Dues & Subscriptions	27,161
Miscellaneous Commodities	6,153
Furniture, Fixtures, & Equipment not Capitalized	86,228
Compensated Absences	(21,558)
TOTAL ADMINISTRATIVE EXPENSES	$ 6,578,420

Supporting Schedule 2

Schedule of Contracted Investment Management Expenses
Year Ended June 30, 2004

FIXED INCOME MANAGERS		
Invesco-National Asset Management Corporation	$ 359,914	
Todd Investment Advisors	365,816	
Total Fixed Income Managers		$ 725,730
EQUITY MANAGERS		
UBS Global Asset Management Corporation	$ 780,000	
Invesco-National Asset Management Corporation	750,000	
Todd Investment Advisors	474,184	
Wellington Management Company	1,398,742	
Total Equity Managers		$ 3,402,926
CUSTODIAN		
Farmers Bank		$ 443,007
CONSULTANT		
Becker, Burke Associates		$ 45,000
TOTAL CONTRACTED INVESTMENT MANAGEMENT EXPENSES		$ **4,616,663**

Supporting Schedule 3

Schedule of Professional Fees for Year Ended June 30, 2004

PROFESSIONAL	NATURE OF SERVICE	YEAR ENDED JUNE 30, 2004
Charles T. Mitchell Company, LLP	Auditing Services	$ 19,000
Mellon Consulting	Actuarial Services	153,609
Reed, Weitkamp, Schell &Vice, PLLC	Attorney Services	10,000
Farmers Bank	Banking Services	23,765
International Claim Specialist	Investigative Services	3,750
	TOTAL	$ 210,124

Charles T. Mitchell Company, LLP
Certified Public Accountants
WILLIAM G. JOHNSON, JR., C.P.A.
JAMES CLOUSE, C.P.A.
BERNADETTE SMITH, C.P.A.
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REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Board of Trustees
Teachers' Retirement System of the State of Kentucky
Frankfort, Kentucky

We have audited the general purpose financial statements of Teachers' Retirement System of the State of Kentucky, a component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2004, and have issued our report thereon dated December 9, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Compliance
As part of obtaining reasonable assurance about whether Teachers' Retirement System of the State of Kentucky's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

Internal Control Over Financial Reporting
In planning and performing our audit, we considered Teachers' Retirement System of the State of Kentucky's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of the audit committee, management, and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

Charles T. Mitchell Co.

December 9, 2004

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